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IN THE

Supreme Court of the United States

October Term, 1973

No. 73-964

In the Matter of

PENN CENTRAL TRANSPORTATION COMPANY,
Debtor,

ALLEN J. GREENOUGH,
Petitioner.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Petitioner, Allen J. Greenough (sometimes erroneously referred to below as "Arthur" J. Greenough), respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit entered in this proceeding on August 21, 1973. Petitioner's petition for a rehearing was denied by order entered October 9, 1973.

Opinions Below

The Reorganization Court's opinion is reported in 354 Fed. Supp. 408. The opinion and Orders Nos. 1087 and 1088 are printed in the Appendix hereto at pages 1A and

28A, respectively. The opinion of the Court of Appeals has not yet been reported and is printed at page 30A of the Appendix hereto.

Jurisdiction

The judgment of the Court of Appeals was entered August 21, 1973 (App. 45A). Rehearing was denied by order entered October 9, 1973 (App. 47A). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and 2102(c).

Questions Presented

1. Whether Petitioner had a vested and secured interest in the Contingent Reserve Fund upon his retirement as an employee prior to the filing of the Debtor's petition for reorganization, which constituted a trust fund for his benefit?

2. Whether the denial of further payment to Greenough of all the moneys deposited to his account in the Contingent Reserve Fund, together with the increments thereto, constitutes an unconstitutional taking of his property without due process of law?

Statute and Constitutional Provisions Involved

The statute involved is Section 77(a) and (l) of the Bankruptcy Act, U.S.C. Tit. 11, Ch. 8, Sec. 205. (Pertinent provisions thereof are printed in App. 48A).

The constitutional provision involved is Amendment No. 5 of the Constitution of the United States (App. 49A).

Statement of the Case

In 1952 the Pennsylvania Railroad, Debtor's predecessor, established a Contingent Compensation Plan ("Plan") for certain of its employees. At that time, Petitioner, Greenough, who had been an employee of the railroad for 24 years, became a participant in the Plan. He worked his way up through the ranks and in 1960 he became President of the railroad. On July 1, 1968 he voluntarily retired from service before the age of 65 years.

Payments in lieu of and equal to what otherwise would have been salary increases were made to the Plan's Contingent Reserve Fund ("Fund") for Greenough's account as a participant and he was notified from time to time of the allotments to his account. When he voluntarily retired on July 1, 1968, the total value of allotments to his account in the Fund was $804,152.59. The Company gave him a statement dated July 15, 1968, showing that valuation as of July 1, 1968 (Exh. G-5, App. 50A).

On November 13, 1968, pursuant to the provisions of the Plan, Greenough elected to receive the full amount of his contingent allotments in annual installments of $100,000.00 each, commencing January 15, 1969 which was six months and fifteen days following the termination of his service (the time prescribed in the Plan), and continuing until the full amount of his share in the Fund was paid.

On November 27, 1968, the Plan's Committee on Organization and Officers' Salaries adopted a resolution that the full amount of Greenough's contingent allotments in the Fund would be paid to him in annual installments of

$100,000.00 each commencing on January 15, 1969, and continuing until the full amount of his interest in the Fund was paid, with the final payment which might be either more or less than $100,000.00, to be paid no later than April 20, 1981 (Exh. G-6, App. 51A).

Pursuant to that resolution $100,000.00 was paid to Greenough on or about January 15, 1969 and $100,000.00 was paid to him on or about January 16, 1970. Under date of April 21, 1970 Greenough was advised by the Secretary of the Company that the total value of his allotments in the Reserve Fund was $625,039.59 (Exh. G-7, App. 52A).

The Debtor's Trustees have refused to pay any further installments to Greenough. By petitions dated December 2, 1971 and December 26, 1972, they applied to the Reorganization Court for authority to settle claims under the Plan, and to liquidate securities in the Fund in an amount not to exceed $10,000,000.00, to deposit the proceeds and to make immediate withdrawals therefrom to meet current operating expenses.

Hearings were held by the Reorganization Court at which counsel for Greenough and other employees, participants in the Plan, were heard, and one record was made of all the hearings. On January 26, 1973, the Reorganization Court issued its Orders Nos. 1087 and 1088.

Order No. 1087 (App. 26A) authorized the Trustees to pay to eligible participants in the "(former) Contingent Compensation Plan of the Debtor amounts determined—in each case by the following formula, viz. (a) the lesser of (i) the total allocations to such participant, or (ii) an amount equal to the value of such participant's share of

the Contingent Reserve Fund as of December 31, 1970, less (b) the aggregate amount of payments heretofore made to such participant or account of his participation." Disposition of further claims of participants in the Plan was deferred pending adoption of a reorganization plan.

Order No. 1087 also adjudged that the assets in the Contingent Reserve Fund are the property of the Trustees free and clear of all claims, legal or equitable, of the participants or former participants in the Contingent Compensation Plan.

Order No. 1088 (App. 28A) authorized the Trustees to liquidate securities in the Fund, to deposit the proceeds, make withdrawals therefrom to meet current operating expenses, and to set aside $2,600,000.00 as a reserve for authorized payments to participants in the Plan. The Trustees were authorized to withdraw $7,400,000.00 of the Fund's assets, which thereby became funds of the Debtor available for current expenses.

Greenough and other affected participants appealed from the said orders to the Court of Appeals for the Third Circuit. That Court heard all of the appeals together and on August 21, 1973 it issued its judgment (App. 45A) and opinion (App. 30A) affirming both orders of the Reorganization Court.

Greenough and other participants petitioned the Court of Appeals for a rehearing, which was denied by the Court by order entered October 9, 1973 (App. 47A).

Reasons for Granting the Writ

The Court of Appeals for the Third Circuit, in affirming the orders of the Reorganization Court has erroneously decided an important question of federal, constitutional law. It has denied Greenough his fully vested right to his share of the Contingent Reserve Fund, a right which vested in him upon his retirement prior to the date the Debtor filed its petition for reorganization. The Fund thereupon constituted a trust fund for Greenough's benefit.

The denial of Greenough's right to the allocations made to that Fund for his account and the increments to his interest in the Fund constitutes an unconstitutional taking of his property without due process of law in violation of the Fifth Amendment of the Constitution of the United States.

These questions are likely to be presented in other reorganization cases, particularly those involving other railroads which are now in reorganization, and settlement of these questions is plainly in the interest of all employees in the employ of those railroads, who have foregone or are foregoing salary increases with the expectation that upon their retirement they would receive the pension payments promised to them and which they believed were assured.

ARGUMENT

I

Greenough's interest in the Contingent Reserve Fund became fully vested and secured upon his retirement prior to the filing of the Debtor's petition for reorganization and constituted a trust fund for his benefit.

When Greenough retired from the railroad company's employ on July 1, 1968, his share of the Contingent Reserve Fund became indefeasibly vested in him. Although his share may have been contingent prior to that date, when he retired, his share, valued as of that date by the Company, became his and his alone, and the Courts below erred in holding that it belonged to the Debtor.

The Courts below have misconstrued Sections 401, 1201 and 1401 of the Plan. It is true that Section 401 states that the Fund shall not be a trust fund and the assets therein shall be available at all times for any corporate purpose of the Company, but that provision cannot be read alone out of context. It must be read in connection with other provisions of the Plan which must be read and construed as a whole. So read, Section 401 is not applicable to a participant once he retires.

Section 1201 of the Plan states that any officer or employee shall have a right to participate in the Plan "to the extent that contingent allotments shall have been made to him in accordance with the provisions of the Plan."

Section 1401 states "that no amendment, suspension, or termination (of the Plan) may without his written consent, apply to the payment to any participant of any contingent allotment previously made to which he would otherwise be entitled."

Section 408 of the Plan provides that upon its termination or suspension there shall be a valuation of the Fund and the contingent allotments of a participant shall be expressed as the amount at which the units were valued and "Upon fulfilling all the conditions of the Plan, such amounts, together with all contingent allotments never represented in the Fund, shall be paid to the participant as hereinafter provided."

Greenough voluntarily retired before age 65. In such case the Committee on Organization and Officers' Salaries could provide that payments to him were to be paid to him in ten annual installments, or in the Committee's sole discretion, at other times in other amounts, or in a lesser or greater number of installments, but in no event could full payment to him be postponed beyond ten years and seven months from the date of the termination of his service.

All provisions of the Plan must be considered in determining its meaning. The law is well established that in construing a writing every part will be considered to give effect to its general purpose.

> "The writing will be read as a whole, and every part will be so interpreted as to give effect to its general purpose."
>
> Williston on Contracts (Third Ed.) Vol. 4, Sec. 618(3).

In *Herryford* v. *Davis,* 102 U.S. 160, this Honorable Court enunciated the rule as follows:

> "What then is the true construction of the contract? The answer to this question is not to be found in any name which the parties may have given to the instrument, and not alone in any particular provision, it contains, disconnected from all others, but in the ruling intention of the parties gathered from all the language they have used. It is the legal effect of the whole which is to be sought for. The form of the instrument is of little account."

Taken as a whole, the Plan indicates that the Committee on Organization and Officers' Salaries, set up under Section 101(d) of the Plan was expressly given the right to pay Greenough the full amount of his allotments at once, in a lump sum when he retired. The Company acknowledged that fact and so advised Greenough. Since he could have gotten it then, it is inconsistent for the Trustees to argue and the Courts below to hold that Greenough now has no right or interest in the Fund.

What the Committee had the right to do should be given the greatest weight in construing Greenough's rights. It is a conclusive reason to give him what he could have received. The total amount allotted to him was and is his as a matter of right.

This position is supported by the Pennsylvania courts. *David* v. *Veitscher Magnesitwerke Actien Gesellschaft,* 348 Pa. 335, was an action to recover pension benefits and dismissal pay which had been established by the defendant's Executive Committee. Defendant pleaded as a de-

fense that a 1938 decree of the German Government cancelled plaintiff's rights. The court rejected that contention and gave judgment to the plaintiff. Chief Justice Maxey, in his opinion, said (p. 342):

> "It is the holding of all of the Pennsylvania cases, which we have cited, that when an employee who is a member of a retirement system, whether it affects policemen, firemen, school teachers or other public employees, has fully complied with all the requirements making him eligible to a retirement allowance, whether he chooses to ask for it then or later, *he has vested right to such allowance which cannot be adversely affected by subsequent legislation,* except for a cause which we will refer to hereinafter. * * *" (emphasis in original)

In *Retirement Board of Allegheny County* v. *McGovern, et al.,* 316 Pa. 161, speaking of retirement pay provided for by statute, the Court stated (p. 168):

> "* * * We said in Busser v. Snyder, 282 Pa. 440, 454, that the basis of retirement pay is neither charitable nor benevolent, but is the faithful valuable service actually rendered over a long period of years. * * *."

and further, on page 169:

> "* * *. The compensation is earned in the present, payable in the future to an employee, provided he possesses the qualifications required by the act, and complies with the terms, conditions and regulations imposed on the receipt of retirement pay. Until an employee has earned his retirement pay, or until the time arrives when he may retire, his retirement pay is but an inchoate right; but when the conditions are satisfied, at that time retirement pay becomes a vested right of which the person entitled thereto cannot be deprived; it has ripened into a full contractual obligation. * * *."

A similar position was stated by the Supreme Court of Ohio in *Cantor* v. *Berkshire Life Ins. Co., et al.*, 171 Ohio St. 405, 171 N.E. 2d 518, where plaintiff, having reached the agreed retirement age, requested permission to retire, which was granted. Shortly thereafter, and after the agreed date of his retirement, the employer attempted to cancel his contract and deprive him of his right to receive further payments. Both lower Courts held that the right to terminate the contract existed by virtue of a provision allowing its termination without cause.

The Ohio Supreme Court reversed and rendered judgment in the plaintiff's favor. In doing so, it stated this significant language (N.E. p. 522):

> "Clearly under our present economic system, an employer cannot offer a retirement system as an inducement to employment and, after an employee has accepted employment under such circumstances, withdraw or terminate the program after an employee has complied with all the conditions entitling him to retirement rights thereunder.
>
> Therefore, whether a retirement plan is contributory or non-contributory and even though the employer has reserved the right to amend or terminate the plan, once an employee, who has accepted employment under such plan, has complied with all the conditions entitling him to participate in such plan, his rights became vested and the employer cannot divest the employee of his rights thereunder.
>
> Plaintiff having complied with all the conditions in his contract entitling him to retirement rights and having reached retirement age under the contract, his retirement right became vested and Berkshire could not terminate his contract so as to divest him of such rights."

There is no question here that Greenough fulfilled all the conditions entitling him to his pension payments under the Plan. While his interest in the amount allotted to him may have been subject to the possibility of loss before his retirement, once he retired his right to those amounts became vested.

Greenough relied on his employer's written promise that if he worked long and faithfully he would ultimately receive the fruits of his labor. He should not and cannot be penalized because he asked to receive his vested, allotted share of the Fund in installments rather than all at once, in a lump sum.

II

The denial of Greenough's right to all the moneys deposited to his account in the Contingent Reserve Fund, together with the increments thereto, constitutes a taking of his property without due process of law in violation of the Fifth Amendment of the Constitution of the United States.

It is conceded that the Bankruptcy Act sanctions the impairment of contract obligations, but it does not sanction the taking of substantive rights in specific property; *Louisville Joint Stock Land Bank* v. *Radford*, 295 U.S. 555, 79 L.Ed. 1593, 55 S. Ct. 854, which passed on the validity of Section 75(s) of the Bankruptcy Act, the Frazier-Lemke Act of June 28, 1934. There, the statute took from the mortgagee, the petitioner, various rights which it had by virtue of its mortgage lien, viz., the right to retain the lien until the indebtedness secured thereby is paid; the right to realize upon the security by a judicial public sale; the right to determine

when such sale shall be held, subject only to the discretion of the Court; the right to protect its interest in the property by bidding at such sale whenever held; and the right to control the property meanwhile during the period of default, subject only to the discretion of the Court, and to have the rents and profits collected by a receiver for the satisfaction of the debt.

Mr. Justice Brandeis, speaking for the Court, said (L. Ed. 1604):

> "The bankruptcy power, like the other great substantive powers of Congress, is subject to the Fifth Amendment. Under the bankruptcy power Congress may discharge the debtor's personal obligation, because, unlike the States, it is not prohibited from impairing the obligation of contracts. * * *. But the effect of the Act here complained of is not the discharge of Radford's personal obligation. It is the taking of substantive rights in specific property acquired by the Bank prior to the Act * * *."

This Court found that the mortgagee had substantive rights under the laws of Kentucky which were interfered with by the Bankruptcy Act.

Petitioner herein, Greenough, had a vested interest in the Contingent Reserve Fund under the law of Pennsylvania (*David* v. *Veitscher Magnesitwerke Actien Gesellschaft*, 348 Pa. 335; *Retirement Board of Allegheny County* v. *McGovern*, 316 Pa. 161, supra.), which was a property right stronger than the lien in Louisville. If deprivation of a mortgagee's lien right is protected from an unconstitutional deprivation, surely Greenough's property right in the Contingent Reserve Fund requires similar protection.

Louisville was followed and cited in *In re Chicago, R.I. & P. Ry. Co.*, 90 F. 2d 312 (CCA-7), cert. den. *Bankers Trust Co.* v. *Wise*, 302 U.S. 717, 82 L.Ed. 554, 58 S.Ct. 37, a railroad reorganization, which stated that a mortgagee's vested rights may not be impaired by Congress and in *Ginsberg* v. *Lindel*, 107 F. 2d 721 (CCA-8).

It is respectfully submitted that the judgment of the Court of Appeals, affirming the orders of the Reorganization Court has deprived Petitioner, Greenough, of a vested property right, in violation of the Fifth Amendment.

Conclusion

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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APPENDIX

Memorandum and Order No. 1087 of the Reorganization Court

IN THE

UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In the Matter of

PENN CENTRAL TRANSPORTATION COMPANY,
Debtor

In Proceedings for the Reorganization of a Railroad

Bky. No. 70-347

MEMORANDUM AND ORDER NO. 1087

[Re: Retirement Programs—Contingent Compensation]

January 26th, 1973

FULLAM, J.

By virtue of various applications and responses thereto, all of which will be detailed later, the Court is required to make comprehensive rulings governing the status of various retirement programs and related programs of the Debtor. A brief description of the programs in question is set forth below; the actual application of each program to particular employees may vary depending upon hiring date and previous employment history:

Memorandum and Order No. 1087

1. *Retirement Programs.* The retirement programs detailed below are designed to complement and supplement employee benefits under the Railroad Retirement Act, 45 U.S.C. §228(a), and for the most part are applicable only to employees not covered by collective bargaining agreements.

(a) *Plan for Supplemental Pensions.* This plan is primarily funded with employee contributions. However, the Debtor makes certain annual contributions to insure the actuarial soundness of the plan. Order No. 278 in these proceedings recognizes that the Debtor had no interest in this fund, which as of April 30, 1972, amounted to $353,521,624. The Debtor does, however, have the right to terminate the program, in which event the fund would be divided among the participants pro rata.

The only issue now before the Court is whether the plan should be terminated. The Debtor's contributions to the program amount to approximately $2 million per year. The Trustees seek authorization to continue the program in operation.

(b) *Suppplementary Benefit Arrangements.* In consequence of the merger between the New York Central and the Pennsylvania Railroad, the Debtor assumed the obligations of two non-contributory plans in effect at the time of the merger: the New York Central supplementary pension plan, and the New Haven pension plan. Under the terms of the respective plans, continuation of the program is optional with the Debtor (NYC ¶¶11 and 12; NH ¶7). The Central plan applies only to those employees who were not entitled to participate in the contributory pension plan of

that railroad and who had 20 years' service. The New Haven plan, applicable to "regular salaried supervisors and officials," was the only pension plan of the New Haven.

Forty-seven employees eligible under the Central plan receive a total of about $23,000 annually, approximately $480 per retiree. Three hundred forty-seven former New Haven employees receive a total of $285,000 per year, approximately $825 per retiree. These amounts are gradually diminishing as a result of attrition.

(c) *Interim or Early Retirement Plan.* This program is designed to facilitate the retirement of selected employees at age 60, rather than at age 65, by assuring total pension benefits equivalent to those which would have been received had retirement been postponed until age 65. Granting of such early retirement is discretionary with the company, but when early retirement has occurred, the company is legally obligated to continue the interim benefits. A similar program, differing somewhat in its mechanics, was inherited from the New York Central in the merger.

For the year 1972, costs to the Debtor under the program amounted to $3,693,000. This cost would decline substantially in future years, unless additional employees are granted early retirement.

Implementation of the early retirement programs produces significant overall economies, making it possible to consolidate certain positions, or to replace highly paid employees with younger, less highly paid substitutes, without the disruptions which would ensue if employees with many years of long and faithful service to the railroad were to be discharged a few years short of retirement. The Trus-

tees estimate that the net savings for the year 1972 amounted to $7.2 million. Projected savings to the year 1980 aggregate some $45 million.

(d) *Additional Pension Benefits.* The Debtor also provides certain additional pension benefits, in two categories: (1) Since 1961, the Debtor has had a policy of crediting prior executive experience with other employers toward the pension entitlements of newly hired executives over 35 years of age earning more than $20,000 annually. The difference between the pension computed with such credit and the pension which would have been paid without such credit is made up from the Debtor's estate. The additional costs under this constructive service policy aggregate approximately $87,000 annually at the present time, and could eventually amount to slightly more than $145,000 annually. The Debtor's constructive service policy follows the universal practice throughout the railroad industry.

(2) Benefits under the Plan for Supplemental Pensions are based upon the employee's average salary over the last five years of employment. Initially, amounts allocated under the Contingent Compensation Plan (*see infra*) were included as salary, for purposes of this computation. However, a 1968 Internal Revenue Service ruling made it necessary to change this policy. Supplement A to the Contingent Compensation Program insures that persons retiring after 1968 will be treated the same as pre-1968 retirees; that is, the Debtor pays the difference between the actual pension benefits and what those benefits would have been if contingent compensation had been included in the computation.

The Trustees propose to continue to carry out all of the foregoing programs.

2. *Contingent Compensation Plan.* This is a complex program under which part of the salary of certain executives, instead of being paid currently in cash, was allotted to them for distribution after retirement. The amounts thus allotted were transferred to a Contingent Compensation Reserve Fund, for investment. This fund now amounts to slightly more than $10 million.

Shortly before the Debtor filed its reorganization petition, the Board of Directors suspended the Contingent Compensation Program, and it remains in suspension to the present date. The details of the program, and the Trustees' proposals with respect to it, will be discussed below.

I. Legal Principles

Resolution of the conflicting contentions of the parties should begin with recognition of the following general principles:

1. Vested, fully funded contributory pension programs are not affected by the employer's filing for reorganization under §77. The assets in any such pension fund are not "property of the Debtor." This much appears to be conceded by virtually all of the parties, and, in any event, has been resolved by Order No. 278 in these proceedings.

2. Irrespective of whether a pension plan is funded or unfunded, continuation of pension payments thereunder is generally treated as a necessary and usual operating expense, payable by the Trustees during reorganization as a cost of doing business. Justification for this practice has been found to arise from the fact that the employee's past

services helped to create and preserve the estate of the Debtor, *e.g., Bowen* v. *Hockley, et al.,* 71 F.2d 781 (4th Cir. 1934), or from the necessity of preserving the loyalty and morale of present and future employees, *see*: *Tate* v. *New York, New Haven & Hartford R.R.,* 332 F.2d 449 (2d Cir. 1964). However, insofar as current payments are concerned, the Trustees have the power to make adjustments in the amount and manner of payment, so long as this is done on an equitable and non-discriminatory basis. *Tate* v. *New York, New Haven & Hartford R.R., supra.*

3. Contractual arrangements for deferred compensation, as distinguished from pension programs, may be disaffirmed by the Trustees, and the claims of employees or former employees resulting from such disaffirmance are not entitled to any special priority or acceleration; the claimants are merely general creditors of the Debtor's estate. *Alpert* v. *New York, New Haven & Hartford R.R.,* 348 F.2d 304 (2d Cir. 1965).

There is thus no difficulty in concluding that the funded pension plan of the Debtor should continue undisturbed, and that the Trustees should continue to make the required contributions. Nor is there any reason for questioning the propriety of the Trustees continuing to carry out the various unfunded pension programs outlined above. These are merely normal operating expenses.

The principal disputes in the present proceeding have to do with the correct treatment of the Debtor's Contingent Compensation Plan, and the legal propriety of imposing a maximum limitation upon the amount payable to any retiree. These issues will be discussed separately.

II. The Contingent Compensation Plan

There are two separate issues, or sets of issues, which must be decided in connection with the Contingent Compensation Program: (1) the status of the Contingent Compensation Fund ("Fund") which was established in connection with this program, and (2) the legal rights of participants in the program (the "Plan"). These issues are, of course, related, in the sense that both the Fund and the Plan must be considered in determining the basic question of whether this is a pension program or some other kind of arrangement; and it is therefore not surprising that the distinctions between the two sets of issues are sometimes obscured in the arguments of counsel. Nevertheless, the distinctions must be kept in mind.

Eligibility for participation in the Plan was limited to salaried employees and officers (except members of the Committee on Organization and Officers' Salaries) designated by the Board of Directors upon recommendation of the Committee. The stated purpose of the Plan was to attract and retain employees in "executive and other key positions." In practice, only persons earning more than $30,000 per year were eligible. A total of 164 employees participated in the Plan (on the date of bankruptcy, the Debtor had more than 92,000 employees, of whom 121 were participants in the Plan).

I agree with counsel for the objecting participants that the express terms of the Plan must be viewed in the light of the manner in which it was implemented. Generally speaking, whenever the union employees of the Debtor obtained

wage increases through collective bargaining, non-agreement employees were given salary increases at approximately the same percentage of increase. And whenever such salary increases became effective, employees participating in the Contingent Compensation Plan received a part of the increase in cash, and the balance was allotted to them under the Plan. The precise apportionment between cash salary increase and allotment to the Plan was carried out on a sliding scale: for participating employees earning between $30,000 and $39,999 annually, 90% of each increase was paid in cash, and 10% went into the Contingent Compensation Plan. For each $10,000 of salary range, these percentages were shifted by 10%, so that, for employees earning $80,000 or more annually, only 20% of each salary increase was paid in cash, and 80% was allotted to the Plan.

Amounts allotted under the Contingent Compensation Plan were treated as operating expenses of the Debtor, but were not reported as compensation paid to the employees, nor were they then taxable as income to the employees.

The Plan provided that, unless otherwise specified by the Committee, allotments accumulated to the credit of a participant would be paid to him, if living, in 10 equal annual installments commencing after his attainment of age 65; or to his designated beneficiary or his estate, in a lump sum. In no case could payment of the full amount of the accumulated allotment be deferred longer than 10 years and 6 months after his death or, in the case of living participants, 10 years and 6 months after attainment of age 65 or severance from employment, whichever was later.

Under the heading "General Description of the Plan," the Plan specifically states "it will normally provide such

individuals with benefits after termination of service *by deferring compensation* until termination of service with the company * * * To achieve this purpose the plan provides *a method of compensating employees*, which differs in several respects from the customary cash payment * * *" [Emphasis supplied]. From this language, from the Plan as a whole, and from the manner in which the Plan was implemented, it is entirely clear that this was a plan for deferred compensation, and not a pension program. Unquestionably, participants in the Plan have valid and subsisting contractual claims against the Debtor's estate. While there are provisions in the Plan for forfeiture, no such forfeiture has ever been asserted in the past, nor does anyone now contend that the participants have forfeited their rights under the Plan. Indeed, the Plan provides, in §1401, "* * * no amendment, suspension, or termination [of the plan] may without his written consent, apply to the payment to any participant of any contingent allotment previously made to which he would otherwise be entitled."

The Contingent Compensation Reserve Fund which was established in connection with the Plan stands, however, on an entirely different footing. Section 401 of the Plan provides:

> "Section 401. The Board may authorize the establishment at any time of a contingent compensation reserve fund, hereinafter called the Fund. The Fund shall not be a trust fund and the assets therein shall be available at all times for any corporate purpose of the company. A participant shall have no right in or to any funds or property which may be held in the Fund."

And in §1201:

> "Section 1201. No participant nor any other person shall have any interest in any fund or in any specific asset or assets of the company by reason of amounts contingently allotted to him. * * *"

And, finally, in §1401:

> "Section 1401 * * * No consent of any participant shall be required, however, in connection with any amendment, suspension or termination of the contingent compensation reserve fund, which shall remain subject at all times to the unrestricted control of the company."

The Board of Directors did set up the Fund, as authorized, but not required, by the Plan. It is apparent that this step was taken in order to achieve two basic objectives: (1) to establish a reserve against the company's contingent liabilities under the Plan; and (2) to provide a mechanism for investing the reserve, and for enabling the participants to obtain the benefits resulting from such investment. Whenever a participant fulfilled all of the requirements of the Plan (*i.e.*, retired and was at least 65 years of age, or died) the total amount payable to him was determined by adding his accumulated allotments which had never been invested in the Fund, to the value represented by his proportionate share of the Fund. In theory, the participants were at risk; if the Fund's investments decreased in value, the participants' deferred compensation might be less than had been allotted to them over the years. As a practical matter, however, the Committee was in a position to terminate the Fund at any time, and presumably would have done

so if faced with any genuine prospect of erosion. Actually, the Fund increased in value over the years; but for the intervention of bankruptcy, the deferred compensation which would have been paid to the participants would in most cases have substantially exceeded the amounts originally allotted.

In view of the provisions of the Plan quoted above, the conclusion is inescapable that the participants have no claim whatever to the reserve Fund as such. The assets of the Fund were "property of the Debtor" on the date of bankruptcy, and are now vested in the Trustees. The objectors nevertheless argue that, in the hands of the Trustees, the assets of the Fund are impressed with a trust, or should be so treated on the basis of equitable considerations. In support of this argument, a number of factors are stressed.

(a) The assets of the Fund were always segregated (but the uninvested contingent allotments were commingled with the general assets of the Debtor for brief periods).

(b) From a balance sheet standpoint, the assets of the Fund, and uninvested contingent allotments, did not contribute to the Debtor's net worth (balancing debits and credits were shown). From this, the objectors contend that no creditor of the Debtor ever relied upon the Fund in extending credit. But this somewhat overstates the case. A creditor who examined the documents establishing the Plan and the Fund would have learned that the Fund assets were unencumbered assets of the Debtor. For present purposes, whether creditors made such inquiry and actually relied

upon these assets in extending credit is not necessarily controlling.

(c) At no time, even in the cash crisis which immediately preceded bankruptcy, did the Debtor see fit to use the Fund for corporate purposes, or to borrow against it. While this can be interpreted as showing that the Debtor's managers considered that these assets were held in trust, it may simply provide some insight into their sense of priorities. Moreover, the action of the Board of Directors, purportedly taken on June 20, 1970 (the day before bankruptcy) terminating all further contingent allotments, and directing that the participants' full salaries should thereafter be paid in cash, is persuasive evidence that all concerned understood the vulnerability of the arrangement in the event of bankruptcy.

The objectors further point out that many of the participants have made commitments, in such matters as estate planning and scale of living, in reliance upon anticipated receipt of contingent compensation pursuant to the Plan. This is undoubtedly a valid consideration. It establishes that the participants, like so many others, relied upon the financial soundness of the Debtor. It provides unnecessary further support for the proposition that the participants have valid claims against the Debtor's estate. But this factor must be balanced against the countervailing equities in determining the extent to which these claims should be satisfied on a current basis during reorganization, rather than in the reorganization plan.

Originally, the Trustees sought authorization to terminate the Contingent Compensation Plan and disaffirm all

obligations thereunder (Document No. 740), thus making the entire fund immediately available for general railroad purposes. Thereafter, recognizing the desirability of improving morale among the present employees, and after extensive negotiations, the Trustees modified their proposal. In their "revised petition * * * concerning Penn Central Transportation retirement programs" (Document No. 1793), the trustees requested leave to continue these programs in effect; and in their "petition * * * for authority to settle claims under the contingent compensation plan" (Document No. 1794), the Trustees sought approval of an agreement embodying the following features: Of the approximately $8.6 million in the Fund as of December 31, 1970, the Trustees would remove approximately $6 million for general railroad purposes, and the balance of $2.6 million would be placed in a reserve fund managed by an independent financial advisor and distributed to the participants according to the terms of the Plan. The proposed allocation of the Fund is calculated to restore to the participants the amounts which they had actually been allotted and had not yet received, or their pro rata share of the Fund as of December 31, 1970, whichever was less (subject, in certain cases, to the $50,000 limitation hereinafter discussed). The participants would not benefit in the growth of the Fund since December 31, 1970. Of the 121 participants in the Plan as of June 21, 1970, 81 agreed to the Trustees' proposal, 33 objected, and 7 expressed no view.

For a variety of reasons, the Trustees' petitions were not immediately acted upon by this Court. The trustees' proposal has now, in effect, been withdrawn, and a further

modification thereof substituted. In the meantime, the Fund has increased to approximately $10 million.

The Trustees' present proposal arises by reason of the prospect of a short-range cash emergency. The Trustees now propose to liquidate all of the assets in the Fund, and use the entire sum for current operating expenses, but to undertake, as an administrative obligation, to pay to participants, as cash permits, the same amounts contemplated by the earlier agreement. A further hearing to consider this proposal was held on January 10, 1973, but the line-up of objectors and proponents remains substantially unchanged. Certain indenture trustees who endorse the legal position taken by the Trustees of the debtor vis-a-vis the participants, pressed further objections to the Trustees' proposed use of the Fund.

Under the Trustees' proposal, the participants would relinquish all claims against the Debtor's estate and the Trustees, except their right to receive amounts equivalent to the unpaid balance of their contingent allotments (or their share of the Fund, as valued as of December 31, 1970). I believe this over-simplifies the issue, and, arguably, cannot lawfully be imposed upon the participants without their consent. While it is true that the participants have no claim to the Fund itself, it is clear that the amounts of their claims under the Plan are to be measured by their pro rata share of the value of the assets in the Fund. The fact that the Committee could lawfully have refrained from investing any of the contingent allotments does not alter the plain langauge of the Plan, to the effect that fluctuations in the value of the Fund investments are to be reflected by equiv-

alent changes (here, increases in most cases) in the participants' respective entitlements under the Plan. (Recognition of the validity of this analysis may be implicit in the inclusion of a "most favored nation" clause in the Trustees' proposed agreement; this would purportedly assure settling participants further payments if the non-settling participants ultimately should fare better than the agreement contemplates.)

Thus, the narrow issue presented is whether, recognizing that all participants have valid lawful claims to the full amount provided for them under the Plan, it would be a proper exercise of discretion to permit present recognition and payment of a portion of each such claim during reorganization, while requiring such claimants to await the adoption of a plan of reorganization before determining the correct treatment of the balance of their claims; and whether the basis on which the Trustees propose to grant such partial recognition is a fair and equitable one.

Since I am satisfied that, strictly speaking, the Trustees would have the right to defer the obligations created by the Contingent Compensation Plan in their entirety, leaving all participants to the proof of claims program, I am satisfied that the participants would have no just cause for complaint if a part of their claims should now be recognized and paid, so long as substantially equal treatment is afforded them. And since I am also persuaded that efficient operation of the railroad requires that employee morale be maintained at a high level, and that capable employees be encouraged to continue in the employ of the railroad, I am likewise satisfied that no creditor or other in-

terest can validly object to the Trustees' proposal to assume the obligation of restoring to the participants the balance of their own 'contributions' under the Plan.

It is correct, as the opponents argue, that under the Trustees' proposal, present employees of the Debtor would receive proportionately larger payments during reorganization (*i.e.*, proportionate to the amounts of their total claims) than would retired participants. This is due to the fact that pre-reorganization payments to retired employees were measured by the full amount of each participant's entitlement; stated otherwise, the retired participants have already received payments which recognized the impact of increased values in the Fund. By the same token, however, the total dollars received by retired participants (in advance of the implementation of a plan of reorganization) will be greater than the amount received by present employees. This, of course, is as it should be, since the retired employees made 'contributions' over a longer period, and in greater amounts, than the present employees.

On balance, I see no inequity in charging amounts which participants have already received from the Contingent Compensation Plan against the amounts which the Trustees will be required to pay in the course of the reorganization.

A further factor bears mention. It is apparent that the Contingent Compensation Plan was carefully drawn with a view toward possible tax consequences. As a general proposition, under the "constructive receipt" doctrine, to the extent that an employee had a non-forfeitable interest in the allotments, the allotments would have been includible in the employee's gross income in the year of the allotment.

See Revenue Ruling 60-31, 1960-1 Cum. Bull. 174; Treasury Regulation 1.451-2; *Doty* v. *U.S.*, 323 F.2d 649 (6th Cir. 1963); *E. T. Sproull* v. *Commissioner*, 16 T.C.C. 244, *aff'd* 194 F.2d 541 (6th Cir. 1952). It is argued that the provisions of the Plan relating to the Debtor's right to use the Fund's assets for corporate purposes were not necessary to secure preferential tax treatment to the participants; but rather, these provisions were included to insure deductibility by the company of contingent compensation allotments at the time payments were made under the Plan. Assuming this to be true, one could hardly criticize management for such action: no inference of overreaching can be drawn. Moreover, nothing in the record negates the natural assumption that the corporate use provisions were included for the independent purpose of having the Fund's assets available should the need arise. I find unacceptable the suggestion that the clear language of the Plan documents should be brushed aside as unimportant because inserted in part for tax purposes. To put the matter in a nutshell, in order to immunize the allotments from current taxation as income of the participants, and to insure deductibility by the employer, the parties set up a program which was vulnerable in bankruptcy. The Trustees' proposals represent a reasonable attempt to mitigate the adverse impact of bankruptcy, while preserving the tax consequences which were bargained for.

A further argument is made by some of the objectors that they were unaware of all of the ramifications of the Contingent Compensation Plan, believed that their 'contributions' were being held for them in trust, and would

have sought employment elsewhere had they known of the true situation. The record does not support these assertions. While it is apparently correct that the participants did not see, and may not have had access to, the documents establishing the Plan, they were furnished, from time to time, summaries of these documents. These summaries appear in the record as follows: Exhibit C-1, dated December 29, 1952; C-2, dated May 20, 1955; C-3, dated January 20, 1956; C-4, dated September 25, 1963; C-5, dated February 1, 1968; and C-6, dated October 1, 1969. I have carefully reviewed all of these informational summaries and find that, while there are some variations in style and emphasis, all fairly and accurately portray the true nature of the Plan, in reasonably brief and non-technical language. In every case, the concluding section plainly states: "The assets of the contingent compensation reserve fund remain assets of the [railroad company] and subject to the rights of all creditors of the company * * *." Moreover, there is actually no evidence in the record that any participant misunderstood the situation.

III. The $50,000 Limitation

By Order No. 12 in these proceedings, I directed that, until further order of Court, no payments be made from the estate of the Debtor to or on behalf of persons no longer employed by the Debtor on a full-time basis, at a rate in excess of $50,000 per annum. This Order remains in effect, and the Trustees propose to incorporate that limitation in the interim arrangements now under discussion.

Memorandum and Order No. 1087

As to six participants in the Contingent Compensation Plan (Messrs. Symes, Greenough, Saunders, Bevan, Perlman and Smucker), the effect of this limitation would be to reduce or eliminate their current participation in the Contingent Compensation Plan, by reason of the amounts being paid them currently under various aspects of the pension program. At the present time, by reason of Order No. 12, no retired employee is receiving more than $50,000 per year, in the aggregate, from the Debtor's retirement and contingent compensation programs. Counsel for all parties appear to be in agreement that participation in the fully funded plan (the Plan for Supplemental Pensions) cannot be thus limited. Mr. Symes is entitled to receive $52,776.12 per year from the funded plan, and Mr. Greenough is entitled to receive $68,478.68 per year from that program. Under the Trustees' proposal Mr. Greenough's contingent compensation would be the value of his units, $222,140.87, less contingent compensation paid, $200,000, or $22,214.08, divided by the appropriate number of payments remaining to be paid under the Plan. The $50,000 limitation would preclude payment of that amount. Mr. Symes is entitled to no contingent compensation under the Trustees' proposal, since he has already received far more than either his original allotments or the value of his units on December 31, 1970. A special $10,000 per year benefit granted Mr. Symes by the Board after his retirement would also be precluded by the $50,000 limitation. Similarly, Mr. Smucker would not receive $5,515 from the unfunded programs that he would otherwise be entitled to, nor would he receive his contingent compensation payment computed at the valuation date of $11,154.15 per annum.

In the case of Mr. Perlman, his entitlement under the funded plan is $41,709.84 per year, which is being paid him. But for the $50,000 limitation, he would be entitled, under the Trustees' proposal, to receive $23,297.22 per year from the Contingent Compensation Plan. Application of the $50,000 limitation would reduce his participation in the Contingent Compensation Plan to approximately $8,200 annually.[1]

In the case of Mr. Bevan, his entitlement under the funded plan is $27,437.27 annually, and under other retirement programs an additional $50,194.24 annually. By reason of the application of the $50,000 limitation, his participation in the unfunded pension programs would be reduced, and his participation under the Contingent Compensation Plan would be eliminated (*i.e.*, insofar as current payments are concerned).

In the case of Mr. Saunders, he is entitled to receive annually $12,247.72 from the funded plan and $78,344.16 from other retirement programs. Application of the $50,000 limitation reduces Mr. Saunders' payments from the unfunded programs and eliminates current participation in the Contingent Compensation Plan. His entitlement under the Trustees' settlement formula would otherwise be $41,200 annually.

In the aggregate, application of the $50,000 limitation would reduce the amount payable on a current basis, under

1. Shortly before reorganization, the Board of Directors entered into a further contract with Mr. Perlman, under which he would have performed services as a consultant, at a salary of $50,000 per year. This contract was disaffirmed by the Trustees before it became effective. Issues arising out of this disaffirmance are not before the Court at this time.

the contingent compensation plan proposal of the Trustees, by approximately $102,000 annually, and would reduce payments from the Debtor's estate under the unfunded retirement programs and otherwise in the amount of about $78,000 for the current year (this latter amount would fluctuate from year to year).

To the extent that the Trustees are required, or find it advisable, to establish a reserve to meet the obligations they propose to assume under the Contingent Compensation Plan, application of the $50,000 limitation would reduce the amount of the required reserve by approximately $1 million.

I have carefully considered all of the arguments advanced on all sides of this question, and have concluded that the $50,000 limitation originally imposed should remain in effect, insofar as that limitation can be achieved through payments within the control of the Trustees. That is to say, while neither the Trustees nor this Court can lawfully interfere with entitlements under the Plan for Supplemental Pensions (the fully funded plan), no payments should be made from the Debtor's estate during reorganization which would, as to any retiree, result in a total post-retirement income from all sources related to the Debtor (*i.e.*, the funded plan, the unfunded retirement programs, and the Contingent Compensation Plan) in excess of $50,000 per year.

In my view, it would be unconscionable to permit the payment in full of all retirement and deferred compensation, no matter how generous the amount, while the Debtor is unable to pay current taxes, or, for example, to pay pre-bankruptcy personal injury claims for which it is legally

liable. Conversely, elimination of all pension and deferred compensation payments from the Debtor's estate would be unduly harsh and, as noted above, would be likely to interfere with the smooth functioning of the railroad. The only acceptable solution is to impose a limitation of some kind.

It has been suggested that the only fair way to impose such a limitation would be on a percentage basis. I reject this approach, believing it would probably involve greater inequities than the flat limitation proposed. Moreover, a percentage reduction might make it difficult for retirees at the lower end of the scale to maintain themselves comfortably, and would permit payments to retirees at the higher end of the scale at unreasonably generous levels. While it is true that the flat $50,000 limitation has a greater dollar impact upon some retirees than others, it assures all retirees of a reasonably comfortable standard of living; moreover, for the most part, the retirees at the higher end of the scale achieved that position as the result of pre-bankruptcy salary policies which are most clearly vulnerable to criticism. On balance, I believe the $50,000 limitation represents an acceptable resolution of these competing considerations.

IV. Implementation

The Trustees originally proposed to set aside increase in the $2.6 million set aside for their benefit.

The arrangement approved herein embodies the following features: (1) the same formula for determining current payments is retained; (2) the validity of the partici-

pants' claims for the full amounts due under the Plan, calculated as of December 31, 1970, is preserved; (3) questions as to the participants' rights to share in the growth of the Fund from December 31, 1970 to the present date remain open for future determination; (4) $2.6 million of the Fund will not be used for operating expenses unless so ordered by this Court in the case of absolute necessity; (5) to the extent that the $2.6 million reserve now being established may grow through investment, and is not used for operating expenses, the Trustees may at some future time be authorized to permit the participants to share in such growth.

I do not now decide that the participants could not lawfully be required to give up all further claims in exchange for current partial payment, but merely that there is room for doubt on the subject, and that the arrangements outlined above seem preferable.

Certain indenture trustees take the position that, while the entire Fund belongs to the Debtor's estate, free of any claims of the participants, it is subject to the lien of the trustees' certificates guaranteed by the federal government, and cannot be used to meet operating expenses except on the strength of a present decision by this Court that the lien of the trustees' certificates, as to encumbered assets of the Debtor, is reduced by that amount. I do not believe that issue is ripe for decision at this time. The government does not object to the Trustees' proposal, and I am satisfied that the use of unencumbered assets to meet operating expenses is entirely consistent with the Emergency Rail Services Act of 1970 (45 U.S.C. §§661-69) and

the terms of the government's guarantee. For this Court now to attempt to forecast all of the possible legal consequences would serve no useful purpose.

V. Conclusions

1. The fully funded Plan for Supplemental Pensions should remain in full force and effect, unimpaired by the Debtor's bankruptcy. The Trustees should be authorized to continue to make contributions thereto, as a cost of doing business.

2. Subject to the limitation hereinafter mentioned, the Trustees should continue to make payments required by the various unfunded pension programs, as a cost of doing business.

3. Participants in the Contingent Compensation Plan have no legal or equitable interest in or claim to the assets in the Contingent Compensation Reserve Fund. Each participant in the Contingent Compensation Plan has a valid claim for the full amount to which he is entitled under the terms of the Plan, but the Trustees should be authorized and directed to recognize such claims during reorganization only to the extent represented by the formula proposed by the Trustees in settlement (*i.e.*, reimbursement of accrued allotments, or pro rata share of the Fund as of December 31, 1970, whichever was less); and such claims should be paid during reorganization only as cash permits. Unless and until otherwise ordered by this Court, the Trustees should set aside and reserve the sum of $2.6 million in order to meet these payments.

4. During reorganization, the Trustees should make no payments from the estate of the Debtor (whether by reason of unfunded retirement programs, or the Contingent Compensation Plan) where the effect of such payment would be that the aggregate amount received by a retired employee from all sources related to the Debtor (*i.e.*, the Plan for Supplemental Pensions, unfunded retirement programs, and the Contingent Compensation Plan) would exceed $50,000 per annum.

Appropriate orders will be entered in conformity with the views expressed herein.

ORDER NO. 1087

Authorizing the Trustees to Carry Out the Provisions of Certain Pension Programs, and to Make Certain Payments on Account of Obligations Arising Under the Contingent Compensation Plan

AND Now, this 26th day of January, 1973, upon consideration of the various Petitions of the Trustees relating to the retirement and contingent compensation programs of the Debtor (Documents Nos. 740, 1226, 1793 and 1794), and after hearings thereon duly noticed, it is ORDERED:

1. The Trustees are authorized to continue in effect the Plan for Supplemental Pensions, in conformity with Order No. 278, and to make all payments required to implement the same.

2. Subject to the limitation set forth in paragraph 5 of this Order, the Trustees are authorized to continue in effect all of the existing pension programs and policies of the Debtor, and to make all payments required to implement the same.

3. Subject to the limitation set forth in paragraph 5 of this Order, from time to time during reorganization, as cash permits, the Trustees are authorized to pay to eligible participants in the (former) Contingent Compensation Plan of the Debtor amounts determined—in each case by the following formula, viz, (a) the lesser of (i) the total allocations to such participant, or (ii) an amount equal to the value of such participant's share of the Contingent

Compensation Reserve Fund as of December 31, 1970, less (b) the aggregate amount of payments heretofore made to such participant or account of his participation. All payments to participants during reorganization shall be made on a pro rata basis in relation to the amounts thus determined. Except as herein provided, disposition of all further claims on behalf of participants in the (former) Contingent Compensation Plan of the Debtor is deferred pending adoption of a reorganization plan.

4. It is adjudged and declared that the assets in the Contingent Compensation Fund are the property of the trustees, free and clear of all claims, legal or equitable, of the participants or former participants in the Contingent Compensation Plan.

5. In no event shall the Trustees make any payment to or on behalf of any former officer or employee of the Debtor where the effect of such payment would be the receipt by such former officer or employee, from the Plan for Supplemental Pensions, all other unfunded retirement programs of the Debtor, and the Contingent Compensation Plan, in the aggregate, of more than $50,000 per annum.

John P. Fullam
J.

Order No. 1088 of the Reorganization Court

IN THE

UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF PENNSYLVANIA

In the Matter of

PENN CENTRAL TRANSPORTATION COMPANY,

Debtor

In Proceedings for the Reorganization of a Railroad

Bky. No. 70-347

ORDER NO. 1088

Authorizing the Trustees to Withdraw $7,400,000 from the Contingent Compensation Reserve Fund

AND Now, this 26th day of January, 1973, upon consideration of the Petition of the Trustees for authority to Withdraw $7,400,000 from the Contingent Compensation Reserve Fund (Document No. 4886), and upon hearing duly noticed, it is ORDERED:

1. Subject to the limitation set forth in paragraph 3 of this Order, the Trustees and Kuhn, Loeb & Co. (as investment manager and custodian of the Contingent Compensation Reserve Fund ("Fund")), are authorized and directed forthwith to liquidate securities or other assets in the Fund (with the exception of the bonds of the Pittsburgh, Cincinnati, Chicago & St. Louis Railroad Company and the 7,500 shares of Madison Square Garden Corporation common stock), free and clear of all liens and encum-

brances, and to deposit the proceeds for the Trustees' account in a bank to be designated by the Trustees.

2. Subject to the limitation set forth in paragraph 3 of this Order, the Trustees are authorized, upon the deposit of said proceeds, to make forthwith withdrawals therefrom to meet current operating expenses.

3. The Trustees shall, until further Order of this Court, reserve and set aside, from the assets of said Fund, or the cash proceeds derived from liquidation thereof, or a combination thereof, assets having an aggregate value of $2,600,000 as a reserve against liabilities which the Trustees may be authorized to pay during reorganization to participants in the (former) Contingent Compensation Plan. The Trustees are authorized to retain appropriate investments in the Fund, or to invest and reinvest said reserve of $2,600,000, in their discretion. Said reserve shall remain the property of the Trustees; establishment and maintenance of said reserve shall not give rise to any legal or equitable interest or claim therein on behalf of any participant.

4. The authority herein granted may be exercised forthwith, irrespective of the pendency of any appeal from this Order or from Order No. 1087 in these proceedings. No stay of this Order will be granted. In the event of a final judicial determination that the authority herein granted should not have been granted, the Trustees' obligation to restore amounts expended pursuant to this Order shall constitute an expense of administration.

John P. Fullam
J.

Opinion of the United States Court of Appeals for the Third Circuit

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

Nos. 73-1081, 73-1098, 73-1204, 73-1205,
73-1206, 73-1207 and 73-1208

In the Matter of: PENN CENTRAL TRANSPORTATION COMPANY, *Debtor*

TWENTY-ONE RETIRED EMPLOYEES,
Appellants in No. 73-1081,

DAVID C. BEVAN, *Appellant in No. 73-1098,*

ALFRED E. PERLMAN, *Appellant in No. 73-1204,*

STUART T. SAUNDERS, *Appellant in No. 73-1205,*

ARTHUR E. BAYLIS, A. M. HARRIS, HENRY W. LARGE, CHRISTY C. MAGRUDER, HERBERT M. PHILLIPS, GEORGE C. VAUGHAN, CAROL JEAN COLE, Executrix of Estate of JAMES B. GRAY, six retired employees and the estate of one retired employee of debtor,
Appellants in No. 73-1206,

ARTHUR J. GREENOUGH,
Appellant in Nos. 73-1207 and 73-1208.

(Bankruptcy No. 70-347)

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Argued May 14, 1973

Before: VAN DUSEN, GIBBONS and ROSENN, *Circuit Judges.*

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OPINION OF THE COURT OF APPEALS

(Filed August 21, 1973)

GIBBONS, *Circuit Judge.*

We here consider consolidated appeals from two orders, Nos. 1087 and 1088 of the Penn Central reorganization court, which deal with the continuation of payments to former Penn Central executives pursuant to several retirement programs. The district court's opinion on these orders is reported. *In the Matter of Penn Central Transportation Company, Debtor,* 354 F. Supp. 408 (E.D. Pa. 1973). Twenty-eight retired Penn Central employees have appealed. The appeals present as issues:

(1) common to all appellants, the propriety of the district court's conclusion that assets held in Penn Central's Contingent Compensation Plan (CCP) became, on the filing of the petition for reorganization, property of the trustees in reorganization, leaving appellants as creditors holding unsecured claims for deferred compensation;

(2) common to six appellants,[1] the propriety of the district court's ruling that the reorganization court would continue payments under the Contingent Compensation Plan as expenses of operation of the reorganization, but with a limitation that total pension payments from the Penn Central Plan for Supplemental Pensions[2] and Penn Cen-

1. Symes, Greenough, Bevan, Saunders, Smucker and Perlman.

2. The Plan for Supplemental Pensions is a funded retirement plan. Order No. 278 held that the trustees had no interest in the fund. Order No. 1087 authorizes the trustees to continue the Plan in existence, making the necessary employer contributions. There is no appeal from this feature of Order No. 1087.

tral unfunded retirement programs,[3] including the Contingent Compensation Plan, would not exceed $50,000 a year to any former employee; and

(3) in the case of Symes, the application of the $50,000-a-year limitation not only to his claim under the Contingent Compensation Plan, but also to his claim under a $10,000-a-year special pension awarded to him by the Penn Central Board of Directors on October 23, 1968. Mr. Symes' case will be dealt with separately hereinafter.

The Contingent Compensation Plan was established by the Board of Directors of the former Pennsylvania Railroad in 1952, was continued after the 1968 merger with New York Central, and was amended, unilaterally, by the Board of Directors from time to time thereafter. When cash salary increases were granted to union employees or to non-union employees not included in the CCP, the qualifying participants were awarded comparable adjustments in compensation, but not in cash. Qualifying participants included employees earning $30,000 or more a year. In its preamble the CCP contains this general description:

"As more fully described below, the Board of Directors, from time to time, may allot to any employee

3. These include two supplementary benefit arrangements of the New York Central, and the New Haven pension plan which Penn Central assumed in the 1968 merger, an Interim or Early Retirement Plan designed to encourage attrition of the labor force, and additional pension benefits for prior service at other railroads. Order No. 1087 authorizes the trustees to continue these plans in effect and to make all payments necessary to implement them. There is no appeal from this feature of Order No. 1087.

an amount representing contingent compensation subject to the terms and conditions set forth herein. At the discretion of the Board an amount equivalent to such allotment, or any part thereof, may be transferred to a reserve fund and invested; and to the extent of such transfer, the payments to a participant shall be measured by the value of the reserve fund. However, the assets held in the reserve fund will at all times be available for any corporate purpose.

After retirement the compensation contingently allotted to a qualifying employe will be paid to him in installments, subject to certain conditions. In the event of death, before or after retirement, payments will be made to the employe's beneficiary."

During the life of the CCP 164 employees were designated by a committee of the Board of Directors as qualifying participants. From 1952, when it was adopted, until June 21, 1970, when by Board action it was terminated, salary increases to the qualifying participants were made in the form of allotments to the CCP. The plan provided for periodic transfer of the allotments to a reserve fund for investment. The extent of such transfer payments to a participant would be measured by the value of the reserve fund. The participants' allotment units would be paid out after his retirement in annual installments, the amount of an installment being determined by reference to the value of his allotment units on the valuation date preceding the date of payment. The CCP contained forfeiture provisions applicable both before and after retirement. With respect to the reserve fund the CCP provided in relevant parts:

"Section 401. The Board may authorize the establishment at any time of a Contingent Compensation Re-

serve Fund, hereinafter called the Fund. The Fund shall not be a trust fund and the assets therein shall be available at all times for any corporate purpose of the Company. A participant shall have no right in or to any funds or property which may be held in the Fund.

Section 1201. No participant nor any other person shall have any interest in any fund or in any specific asset or assets of the Company by reason of amounts contingently allotted to him, nor any right to receive any distribution under the Plan except as and to the extent expressly provided in the Plan * * *.

Section 1401. * * * No consent of any participant shall be required, however, in connection with any amendment, suspension or termination of the Contingent Compensation Reserve Fund, which shall remain subject at all times to the unrestricted control of the Company."

From time to time Penn Central distributed to qualifying employees descriptive summaries of the CCP. Typical of the relevant language of such summaries is the description from the one dated October 11, 1969:

"Either the contingent allotments or the Fund may be discontinued at any time at the discretion of the Board, however, in either instance employes' rights remain whole for the period prior to such termination date.

The assets of the Contingent Compensation Reserve Fund remain assets of the Penn Central Transportation Company and subject to the rights of all creditors of the Company. No participant has any right to receive payments at any other times or in any other amounts than as provided by the Plan."

Opinion

When, shortly before the filing of the petition for reorganization, the Penn Central directors terminated the CCP, the Contingent Compensation Reserve Fund contained in excess of $8.6 million. Of this sum, a substantial amount represented appreciation in the fund investments over the initial allotments made on account of the participants' services. Further appreciation took place after the filing of the petition for reorganization, so that when the district court made the rulings appealed from the Fund was valued at over $10 million.

Originally the trustees petitioned the reorganization court for authorization to disaffirm all obligations under the CCP and to expend the entire Contingent Compensation Reserve Fund for general railroad purposes. Thereafter, recognizing that such a result could adversely affect the morale of those qualifying participants who were still employed by the railroad, the trustees filed a revised petition seeking approval of a proposed settlement with the CCP claimants. Under this proposed settlement, $2.6 million of the Fund balance would be placed in a reserve fund managed by an independent financial advisor and would be distributed to the participants in proportion to their allotment units, but with the value fixed at the amounts actually allotted but not yet received, or at the value of the pro rata shares of the Fund as of December 31, 1970, whichever was less, and all subject to a $50,000 limitation per person per year. The proposed settlement had other features which need not be alluded to because for a number of reasons the offer was withdrawn, and the matter proceeded to hearing on a revised trustees' proposal. That proposal was to liqui-

date the entire Fund, to use the entire Fund for operating expenses, but to pay the participants, as an administration expense, as cash permitted, the amounts proposed in the earlier settlement proposal. The trustees contemplated that such an undertaking by them would be conditioned upon the relinquishment by the participants of any rights to receive payments beyond their actual allotments (or their share in the Fund valued as of December 31, 1970, if that was lower).

The district court did not go so far as the trustee proposed. The court's conclusions here challenged were:

> "3. Participants in the Contingent Compensation Plan have no legal or equitable interest in or claim to the assets in the Contingent Compensation Reserve Fund. Each participant in the Contingent Compensation Plan has a valid claim for the full amount to which he is entitled under the terms of the Plan, but the Trustees should be authorized and directed to recognize such claims during reorganization only to the extent represented by the formula proposed by the Trustees in settlement (*i.e.*, reimbursement of accrued allotments, or pro rata share of the Fund as of December 31, 1970, whichever was less); and such claims should be paid during reorganization only as cash permits. Unless and until otherwise ordered by this Court, the Trustees should set aside and reserve the sum of $2.6 million in order to meet these payments.
>
> 4. During reorganization, the Trustees should make no payments from the estate of the Debtor (whether by reason of unfunded retirement programs, or the Contingent Compensation Plan) where the effect of such payment would be that the aggregate amount received by a retired employee from all sources related to the Debtor (*i.e.*, the Plan for Supplemental Pensions,

> unfunded retirement programs, and the Contingent Compensation Plan) would exceed $50,000 per annum." 354 F. Supp. at 419.

This disposition of the Fund was implemented by Order No. 1088, and a stay was denied both by the district court and by this court. All but $2.6 million has now been expended for general railroad purposes. While Order No. 1088 provides that this sum be invested as a reserve to meet the payments to participants contemplated by the decision, it also provides:

> "Said reserve shall remain the property of the Trustees; establishment and maintenance of said reserve shall not give rise to any legal or equitable interest or claim therein on behalf of any participant."

Summarizing, then, the orders appealed from (1) relegated qualifying participants in the CCP to the status of unsecured creditors, to be dealt with in the plan of reorganization in some as yet undetermined manner, (2) authorized the trustees to treat the participants' claims as in the nature of unfunded pension liabilities and to pay these, in reduced amounts, as current operating expenses, and, (3) set aside from the $10 million Contingent Compensation Reserve Fund $2.6 million as a reserve from which to meet those operating expenses. The reserve was recognized to be a matter of grace, however, and subject to reconsideration by the reorganization court.

It is common ground between the appellants and the trustee-appellees that in a railroad reorganization, some payment on account of unfunded pension liabilities by the trustees are properly treated as necessary and usual operating expenses and as a cost of doing business. In *Tate* v.

New York, New Haven & Hartford R.R., 332 F.2d 440 (2d Cir. 1964), the Second Circuit justified such payments as necessary to preserve the morale of present and future employees. In *Bowen* v. *Hickley*, 71 F.2d 781, 785-86 (4th Cir. 1934), the practice was justified on the ground that the pensioners' past services helped to create and preserve the estate being administered. Apparently payment of unfunded pension liabilities during a railroad reorganization is a recognized tradition in the industry. *See* Myers, *Financial Impact of Pension Costs on the Railroad Industry*, 7 Lab. L.J. 265, 266 (1956). *Compare In re Compania De Los Ferrocarriles De Puerto Rico*, 76 F. Supp. 521 (D.P.R. 1948). *Cf. Alpert* v. *New York, New Haven & Hartford R.R.*, 348 F.2d 304 (2d Cir. 1965) (distinguishing deferred compensation contracts from pensions). This court has not explicitly ruled on the practice. Since no party to this appeal challenges it, we accept it, for present purposes, as a governing rule. Nor do we reach in this case any issue as to the ultimate priority, if any, to which the CCP claimants may be entitled in a reorganization plan. This appeal deals only with the district court's rejection of appellants' contentions as to their present rights in the Contingent Compensation Reserve Fund. These contentions are:

(1) that the CCP should be regarded as a funded rather than as an unfunded pension plan, (or as the trustees prefer, deferred compensation plan) and that the trustees have no interest in the Fund;

(2) that at least as to those participants who retired prior to termination of the CCP, their claims should be treated as vested and secured;

(3) that the reduction in benefits resulting from the refusal of the court to give effect to appreciation in the Fund beyond the original allotments is inconsistent with the practice, referred to above, of recognizing pension liabilities during a railroad reorganization; and

(4) that the $50,000 per annum ceiling on pension payments during reorganization is discriminatory and improper.

In support of their contention that the CCP should be regarded as a funded rather than an unfunded pension plan, appellants argue that the Contingent Compensation Reserve Fund was a trust; express, constructive, or resulting. The Plan provisions quoted above, the Plan as a whole, and all the documents in the record referring to it negate any intention on the part of the Pennsylvania or Penn Central Directors to create an express trust. *See* Restatement (Second) of Trusts §2 (1959). Since there was neither an express trust which failed nor a transfer of property paid for by another, there could be no resulting trust. Restatement (Second) of Trusts, Chapter 12 (1959). Had the Fund, while held by Penn Central, been held in a trust capacity, there would be room for argument that the reorganization trustees became constructive trustees. Restatement of Restitution §160 (1937). But where, as here, the Plan made clear that the Fund was held as a part of the company's general assets, subject at all times to its use and disposition, and subject to the claims of its creditors, there is no basis from which a constructive trust could be implied. The CCP was, as the district court found, nothing

more than an executory contract calling for compensation after retirement.

Nor can any distinction be made between those participants retired prior to termination of the CCP and those still employed thereafter. The Plan itself makes no such distinction. Even the amount to be paid remains uncertain until the valuation date immediately prior to the payment. Moreover, the benefits remain forfeitable even after retirement if the retiree does not refrain from activities adversely affecting the company's best interests. *Compare* the Plan *with Retirement Board* v. *McGovern,* 316 Pa. 161, 174 A. 400 (1934). But in any event, appellants' argument that their rights "vested" upon retirement is entirely beside the point. Their rights may well be "vested"; they are nevertheless unsecured. The issue remains: how should "vested" executory contract pension rights be treated during a railroad reorganization?

Accepting, as have the parties, the general principle that some payments of unfunded pension liabilities are a practical necessity if a railroad is to be successfully operated in reorganization, it does not follow that in applying the principle the reorganization court must enforce each executory pension contract exactly in accordance with its terms. We are dealing with the powers of a court of equity to deal practically with the ongoing problems of employee morale, retention and recruitment. Even looked upon as an equitable recognition of the contributions made to the creation and preservation of the estate, the practice does not necessitate confining the court to the straight jacket of the underlying contract. Indeed, one can envisage a situation where recognizing the exact terms of an unfunded

pension contract might both have an adverse effect upon morale of present and future employees and be inconsistent with any contribution made to the debtor's estate. Accepting the principle of some payment of unfunded pension liabilities, no more is required than a responsible exercise of equitable discretion. We find no abuse of discretion in Order No. 1087.

What we have said about the court's equitable discretion with respect to the treatment of payments based upon appreciation in the Contingent Compensation Reserve Fund applies as well to the $50,000-a-year limit. The district court found as a fact that this level of pension would afford each of the participants a decent living standard. We will not second guess his well-considered judgment that no more was appropriate during the pendency of the reorganization.

Finally, there is the separate contention of appellant Symes that the court erred in refusing to continue payment, during reorganization, of a special pension of $10,000 a year voted by the Board of Directors on October 23, 1968. Order No. 1087 makes no final disposition of Mr. Symes' claim on this special arrangement, but it is subject to the overall limitation of $50,000 a year, and Mr. Symes' pensions from other Penn Central sources exceed this amount. For purposes of payment during reorganization, nothing distinguishes the October 23, 1968 unfunded pension contract from the other unfunded pension contracts dealt with in Order No. 1087.

We emphasize that because the parties agree that some payments on unfunded pension liabilities during a railroad reorganization are at least proper, this opinion has not

dealt definitively with questions of the extent of or the limitations upon the reorganization court's power in this respect. We also emphasize that the orders appealed from do not determine how the appellants' claims should be dealt with in a plan of reorganization or a liquidation.

Orders No. 1087 and 1088 will be affirmed.

VAN DUSEN, *Circuit Judge*, dissenting in part:

I respectfully dissent only insofar as the majority opinion fails to grant to James M. Symes any part of the $10,000. per year special pension granted on October 23, 1968, after over 50 years[1] of exceedingly valuable service to the Pennsylvania Railroad. The record, including the Appendix, submitted with respect to this special pension, establishes that the principles of equity and fairness require the payment of all or part of this pension to him for the reasons stated in part II of the brief filed on his behalf concerning this special pension. I would vacate that portion of paragraph 5 of Order 1087 which denies completely this pension and remand with directions that the $10,000. per year special pension be paid to Mr. Symes for the period since June 21, 1970.

In all other respects, I concur in the majority opinion.

A True Copy:

Teste: THOMAS F. QUINN
Clerk of the United States Court of
Appeals for the Third Circuit.

---

1. 47 years and 3 months of continuous active service and approximately 6 additional years as a director prior to his retirement.

Judgment of the United States Court of Appeals for the Third Circuit

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 73-1081, 73-1098, 73-1204/73-1208

In the Matter of:

PENN CENTRAL TRANSPORTATION COMPANY, Debtor

Twenty-one retired employees of the Debtor,
Appellants in No. 73-1081

David C. Bevan, Appellant in No. 73-1098

Alfred E. Perlman, Appellant in No. 73-1204

Stuart T. Saunders, a former
employee of the Debtor, Appellant in No. 73-1205

Arthur E. Baylis, A. M. Harris,
Henry W. Large, Christy C. Magruder,
Herbert M. Phillips, George C. Vaughan,
Carol Jean Cole, Executrix of Estate
of James B. Gray, six retired
employees and the estate of one retired
employee of debtor, Appellants in No. 73-1206

Allen J. Greenough,
Appellant in Nos. 73-1207 and 73-1208

(D. C. No. B-70-347 In Bankruptcy)

On Appeals from the United States District Court
for the Eastern District of Pennsylvania

Present:

VAN DUSEN, GIBBONS and ROSENN, *Circuit Judges.*

Judgment

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the orders of the said District Court filed January 26, 1973, be, and the same are hereby affirmed, with costs taxed against appellants.

Attest:

THOMAS F. QUINN
Clerk

August 21, 1973

Sur Petitions for Rehearing

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

Nos. 73-1081, 73-1098, 73-1205, 73-1207 and 73-1208

In the Matter of:

PENN CENTRAL TRANSPORTATION COMPANY, Debtor

TWENTY-ONE RETIRED EMPLOYEES,
Appellants in No. 73-1081

DAVID C. BEVAN, Appellant in No. 73-1098

STUART T. SAUNDERS, Appellant in No. 73-1205

ARTHUR J. GREENOUGH,
Appellant in Nos. 73-1207 and 73-1208

(Bankruptcy No. 70-347)

Sur Petitions for Rehearing

Present:

SEITZ, *Chief Judge*, VAN DUSEN, ALDISERT, ADAMS, GIBBONS, ROSENN, WEIS and GARTH, *Circuit Judges*

The petitions for rehearing filed by Appellants in the above entitled case having been submitted to the judges who participated in the decision of this court and to all the other available circuit judges of the circuit in regular active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular active service not having voted for rehearing by the court in banc, the petitions for rehearing are denied.

By the Court,

JOHN J. GIBBONS
Judge

Dated: October 9, 1973

Pertinent Provisions of the Bankruptcy Act, Section 77(a) and (l), 11 U.S.C. 205(a) and (l)

"205. Reorganization of Railroads Engaged in Interstate Commerce—

(a) Any railroad corporation may file a petition stating that it is insolvent or unable to meet its debts as they mature and that it desires to effect a plan of reorganization * * *. If the petition is so approved, the court in which such order is entered shall, during the pendency of the proceedings under this section and for the purposes thereof, have exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it had appointed a receiver in equity of the property of the debtor for any purpose * * *."

"(l) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the Court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition was filed."

United States Constitution—Amendment No. 5

"No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

Goodstein Exhibit G-5

Statement Dated July 15, 1968 Sent to Allen J. Greenough

[LETTERHEAD OF]

PENN CENTRAL
Six Penn Central Plaza
Philadelphia, Pa. 19104

July 15, 196

Mr. A. J. Greenough, President
Pennsylvania Terminal Real Estate Company
230 Park Avenue
New York, N. Y.

As of July 1, 1968, your contingent compensation under the term and conditions of The Contingent Compensation Plan was represente as follows:

	Unit Value 6/30/68	*Units in Fund*	*Aggregate Amount Represented in Fund*	*Cash not in Fund*	*Total Value o Continge Allotmen*
Series A	$106.29	3,996	$424,718.45		$424,718.4
Series B	$115.67	3,280	379,390.02	$44.12	379,434.1
Total		7,276	$804,108.47	$44.12	$804,152.5

/s/ BAYARD H. ROBER

Goodstein Exhibit G-6

Resolution Dated November 27, 1968 Regarding Payment of Contingent Allotments to Allen G. Greenough

PENN CENTRAL COMPANY

November 27, 1968

Dear Sir:

At a meeting of the Committee on Organization and Officers' Salaries, held this day, the following action was taken:

RESOLVED that payment be made to A. J. Greenough of the full amount of his contingent allotments in the following manner:

annual installments of $100,000. each commencing on January 15th, 1969, and continuing until the full amount of his interest in the fund shall have been paid, provided that final payment (which may be either more or less than $100,000.) shall be made no later than April 20th, 1981.

Yours truly,

/s/ BAYARD H. ROBERTS
Secretary

Mr. A. J. Greenough

Goodstein Exhibit G-7

Letter to Allen J. Greenough from Secretary of the Company Dated April 21, 1970

[LETTERHEAD OF]

PENN CENTRAL
Office of the Secretary
Six Penn Central Plaza
Philadelphia, Pa. 19104

April 21, 1970

Mr. A. J. Greenough
Round Island
Greenwich, Connecticut 06830

Dear Mr. Greenough:

As of April 1, 1970 your contingent compensation under the terms and conditions of The Contingent Compensation Plan of Penn Central Transportation Company was represented as follows:

	Unit Value 3/31/70	*Units in Fund*	*Aggregate Amount Represented in Fund*	*Cash not in Fund*	*Total Value of Contingent Allotments*
Series R	$69.64	8,975	$624,983.32	$56.27	$625,039.59

Sincerely,

/s/ BAYARD H. ROBERTS
Secretary

October Term, 1973

Nos. 73-854, 73-964, 73-1039

IN THE MATTER OF

PENN CENTRAL TRANSPORTATION COMPANY,
Debtor

DAVID C. BEVAN, *Petitioner in No. 73-584*
ALLEN J. GREENOUGH, *Petitioner in No. 73-964*
TWENTY-ONE RETIRED EMPLOYEES,
Petitioner in No. 73-1039

v.

TRUSTEES OF PENN CENTRAL TRANSPORTATION COMPANY

BRIEF FOR RESPONDENTS IN OPPOSITION

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Goncer M. Krestal
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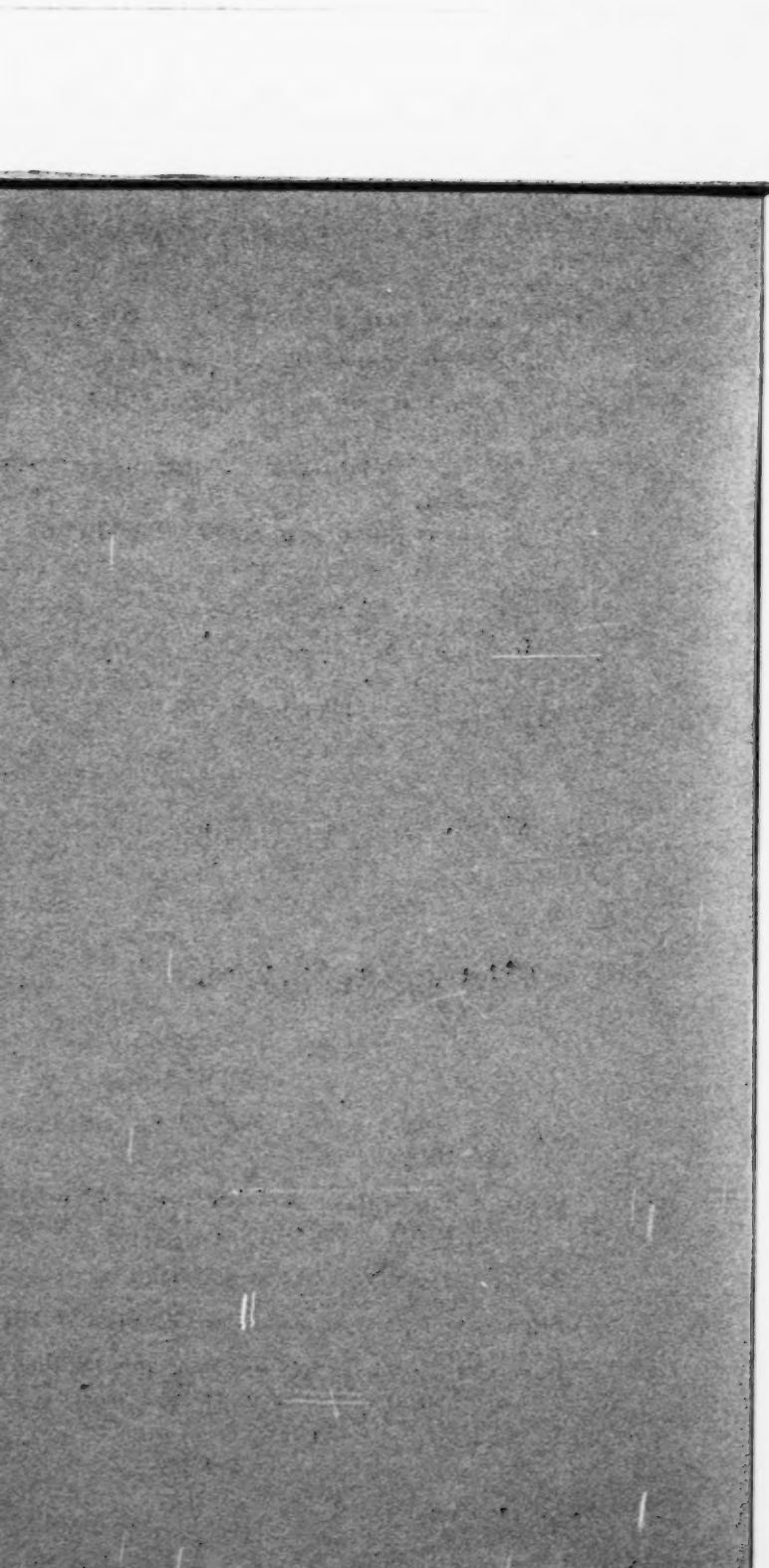

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1 Scott, Trusts §23, at pp. 190-91, §74.3, at p. 682 (3d ed. 1967) 14

COUNTER-STATEMENT OF ISSUES PRESENTED

1. Did the United States District Court for the Eastern District of Pennsylvania (Reorganization Court) in the proceedings for the reorganization of Penn Central Transportation Company (Penn Central) properly exercise its discretion in denying preferential payment to the participants of The Penn Central Contingent Compensation Plan (CCP) of the entire amounts due them under the CCP on account of services rendered to Penn Central prior to the institution of the reorganization proceedings?

2. Are the assets of the Contingent Compensation Reserve Fund (Reserve Fund) maintained by Penn Central for the purpose of meeting its obligations under the CCP to retired participants the property of the Trustees of the Property of Penn Central (Trustees), free and clear of any claims of the participants, in view, *inter alia*, of the express language of the CCP which provides:

> The Fund shall not be a trust fund and the assets therein shall be available at all times for any corporate purpose of the Company. A participant shall have no right in or to any funds or property which may be held in the Fund?

3. Did the Reorganization Court properly exercise its discretion in imposing a $50,000 per annum limitation upon the payment of unfunded retirement benefits to each of six retired highly paid executives of Penn Central?

COUNTER-STATEMENT OF THE CASE

The instant matter arises out of the affirmance by the United States Court of Appeals for the Third Circuit (Court of Appeals) of Order No. 1087 of the Reorganization Court. Order No. 1087 authorizes the Trustees:

> (1) to continue in existence, and to make payments to retired employees under, Penn Central's several funded and unfunded retirement programs;
>
> (2) to make partial payments during reorganization, in the approximate total amount of $2.6 million, as cash permits, to the participants of the CCP, in accordance with a formula approved by the Trustees and accepted by 81 of the 121 participants, without prejudice to the further determination of the participants' claims for payment of their full accounts in the CCP; and
>
> (3) To make additional contributions to the independent trust which funds the Penn Central Plan for Supplemental Pensions (Supplemental Pension Plan).

The payments to be made by the Trustees under Order No. 1087 are subject to an express condition limiting the annual unfunded benefits receivable by anyone of Penn Central's former employees under all of the retirement programs and the CCP to $50,000 per year.[1] This limitation applicable to only six of Penn Central's former executives, does not affect payment of benefits in excess of $50,000 solely out of the funded Supplemental Pension Plan.[2]

---

1. The limitation was originally imposed by the Reorganization Court by Order No. 12, dated July 10, 1970, which was applicable to all pensions payable to retired employees, including payments out of the Supplemental Pension Plan.

2. As a consequence, the annual pensions payable to petitioners Symes (No. 73-1039) and Greenough (No. 73-964) under the Supplemental Pension Plan, which were reduced to $50,000 by Order No. 12 of the Reorganization Court, have been reinstated to the full amounts ($52,776.12 in the case of Symes and $68,478.60 in the case of Greenough) due them under the Plan.

The Reorganization Court, in Order No. 1087, further declared that the assets of the Reserve Fund established under the CCP, having an approximate value of $10 million, were the property of the Trustees, free and clear of any claims by the participants, and in an accompanying Order, No. 1088, directed the liquidation of the Reserve Fund. Order No. 1088 required the Trustees to set aside in reserve out of the assets or proceeds of the Reserve Fund the amount of $2.6 million to meet the payments authorized under Order No. 1087, and authorized the Trustees to utilize the remaining $7.4 million to meet current expenses of operating Penn Central's railroad.

Both the Reorganization Court and the Court of Appeals refused to stay the liquidation authorized under Order No. 1088. As a consequence, the Reserve Fund has been liquidated and the proceeds have been applied in accordance with Order No. 1088, *i.e.*, $2.6 million has been reserved for the participants and the balance has been expended for current operating expenses.

Appeals were taken from Orders No. 1087 and 1088 on behalf of 32 retired executives of Penn Central, or estates of deceased executives, who were participants in the CCP, including the six individuals affected by the $50,000 limitation. These appeals were consolidated for argument before the Court of Appeals and, on August 21, 1973, the Court of Appeals rendered a decision affirming Orders Nos. 1087 and 1088. In this respect, the Court of Appeals expressly held that the assets of the Reserve Fund were not trust funds and that the participants in the CCP merely had unsecured claims against the Penn Central estate for the amount of their interests in the plan. It was further determined that the Reorganization Court had not abused its discretion by limiting the payment out of the estate of unfunded benefits due retired employees of Penn Central both under the CCP and Penn Central's other retirement programs.[3] Applications for rehearing were denied by the Court of Appeals on October 9, 1973.

3. One judge dissented in part only insofar as the Reorganization Court had denied payment to one of the appellants, petitioner

There is presently before this Court a total of three petitions for writs of certiorari, involving twenty-three petitioners, seeking review of the Court of Appeals' decision. This brief is submitted in response to all three petitions.

The facts with respect to Penn Central's retirement programs, the CCP and the effect of the $50,000 annual limitation upon the payment of retirement benefits are as follows:

A. *Facts Relating to Penn Central Retirement Programs*

Although the CCP provides payments to the participants after their retirement, it is not the exclusive, nor the primary, source of retirement benefits payable to retired employees of Penn Central. On the contrary, it is a program the participation in which was limited to a select group of highly compensated executives of Penn Central which was established for purposes different than those giving rise to the normal pension plan. The retirement benefits payable under the CCP are merely incidental to its primary purpose of deferring receipt of a portion of the participants' compensations and are supplemental to the retirement benefits payable to the participants both under the Railroad Retirement Act, 45 U.S.C. §228(a), and under Penn Central's general retirement programs.

Aside from the Railroad Retirement Act, which covers all of Penn Central's employees, the basic pension plan applicable to Penn Central's employees, principally those not covered by collective bargaining contracts, is the funded Supplemental Pension Plan. The benefits under this Plan, are payable out of a trust funded primarily by contributions made by Penn Central and its predecessors.

Note 3—*Continued*

James M. Symes (No. 73-1039), of a special pension of $10,000 a year, in addition to his pension of $52,776 payable under the Supplemental Pension Plan, awarded several years *after* his retirement.

The Supplemental Pension Plan is augmented by a number of other programs which are more limited in scope and coverage and which provide benefits payable directly by Penn Central. These include, insofar as relevant hereto:[4]

> (a) The Policy of June 28, 1961, which provides retirement benefits, in addition to those payable under the Supplemental Pension Plan, to employees whose employment began subsequent to their thirty-fifth birthday and who earned $20,000 or more a year to reflect prior service (up to a maximum of twenty years) with another railroad or other company.
>
> (b) Supplement A to the CCP which provides retirement benefits, also in addition to those payable under the Supplemental Pension Plan, to participants of the CCP who retired between August 1968 and June 1970 based upon the participants' contingent compensation allotments.

Almost all of the petitioners continue to receive substantial pensions under the Supplemental Pension Plan based upon their years of service and compensation, and a number further receive additional benefits under one or more of the other Penn Central retirement programs. No appeal has been effected from that portion of Order No. 1087 authorizing the continuation of these programs.

B. *Facts Relating to Contingent Compensation Plan*

The CCP was established by Penn Central's predecessor, The Pennsylvania Railroad Company, on November 26, 1952. Under the CCP, Penn Central awarded to those employees selected as participants, limited to executives

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4. The remaining unfunded retirement plans maintained by Penn Central are as follows: New York Central Railroad Company unfunded Supplementary Pension System; New York, New Haven and Hartford Railroad Company unfunded pension plan; Penn Central Interim Pension Policy.

and professionals having annual cash salaries in excess of $30,000, allotments of contingent compensation in addition to their regular salaries. This contingent compensation was not payable immediately in cash but rather in ten annual installments after the termination of the participant's employment or attainment of age 65, whichever was later, or in a lump sum or installments (depending upon time of death) to the participant's beneficiary or estate upon death. Until paid, all amounts allocated under the CCP are subject to forfeiture under certain circumstances. Amounts allotted under the CCP were treated as operating expenses of Penn Central but were not reported as compensation paid to the participants, nor were they then taxable as income to the participants.

The CCP authorized, *but did not require*, the establishment of the Reserve Fund, as a separate fund to be maintained by Penn Central into which amounts equal to the contingent compensation allotments could be transferred for the purpose of investment and providing a source for the payments to participants when due under the CCP. The Reserve Fund was established concurrently with the adoption of the CCP and amounts equal to the contingent compensation allotments were transferred thereto monthly by Penn Central. All of the assets of the Reserve Fund were derived solely from these monthly payments by Penn Central. *No monies were ever paid to the Reserve Fund by the participants.*

Under the CCP, the amount of each participant's interest in the Plan was stated in terms of units of the Reserve Fund, the value of which would increase or decrease depending upon the growth of the fund by way of income and unrealized gain. All payments to be made to a participant at retirement were to be based upon the value of the participant's units in the CCP at the time of payment.

In June 1970, the Board of Directors of Penn Central suspended the operation of the CCP and no further contingent compensation allotments have been allocated to the participants since that time. Moreover, since the institution

of the reorganization proceedings on June 21, 1970, no payments have been made out of the Reserve Fund to the participants.

Order No. 1087 provides for the payment to the participants of that portion of their interests in the CCP as of December 31, 1970 equal to the principal amount of their contingent compensation allotments less any payments previously made under the Plan, subject to the $50,000 per annum limitation. The balance of the participants' interests in the CCP represents the appreciation in value of the investment of the Reserve Fund together with most of the unpaid contingent compensation allotments of the six participants whose annual payments are restricted to $50,000.

The petitioners herein were high salaried executives, most of whom participated in the CCP from its inception and whose accounts in the Plan increased substantially in value over the amount of their contingent compensation allotments as a result of the favorable investment by Penn Central of the assets of the Reserve Fund. In some cases, the sums already distributed to these participants far exceed the amounts originally allocated to their accounts.

C. *Facts Relating to $50,000 Per Annum Limitation*

The $50,000 per annum limitation upon the payment of unfunded retirement benefits imposed by the Reorganization Court affects only six former executives of Penn Central, four of whom are petitioners herein. The effect of Order No. 1087 on the payment of benefits to these four individuals is as follows:

1. James M. Symes (No. 73-1039)

Under Order No. 1087, petitioner Symes is entitled to receive his full benefits under the funded Supplemental Pension Plan in the annual amount of $52,776.12. The $50,000 limitation affects the current payment of an additional $10,000 pension awarded to him five years after

retirement and which is *not* funded. Mr. Symes was further denied preferential payment of the $190,505 remaining in his account in the CCP. This results both from the $50,000 per annum limitation and from the fact that the payments to him under the Plan prior to reorganization, $440,451.64, far exceeded the amount of his allotments, $251,096.23.

2. David C. Bevan (No. 73-854)

Under Order No. 1087, the annual benefits payable to petitioner Bevan have been limited to $50,000, of which $22,562.76 is paid by Penn Central directly from current operating receipts, the balance of $27,437.28 being paid under the funded Supplemental Pension Plan. The principal effect of this limitation is to reduce the benefits currently paid to Bevan under the Policy of June 28, 1961 and Supplement A to the CCP and to eliminate current payments to Bevan of the sums credited to his account in the CCP.

2. David E. Smucker (No. 73-1039)

Under Order No. 1087, the annual benefits payable to petitioner Smucker have been limited to $50,000, of which $9,693.96 is paid by Penn Central directly from current operating receipts, the balance of $40,306.08 being paid under the Supplemental Pension Plan. The principal effect of this limitation is to reduce minimally the unfunded retirement benefits currently paid Smucker under Supplement A to the CCP and to eliminate all current payments to him under the CCP.

4. Allen J. Greenough (No. 73-964)

Under Order No. 1087, petitioner Greenough is entitled to receive his full pension under the Supplemental Pension Plan in the annual amount of $68,478.60. The $50,000 limitation affects only the current payment of that portion ($22,140.87) of Mr. Greenough's contingent compensation allotments, which were in the total sum of $222,140.87, in excess of the $200,000 already paid to him

under the CCP prior to reorganization. Mr. Greenough was further denied preferential payment of the balance of his interest in the CCP, in the amount of $541,335.55, representing increases in the value of the Reserve Fund, on the basis of the formula applicable generally to the participants.

REASONS FOR DENYING THE WRIT

1. The Reorganization Court Properly Exercised Its Discretion in Denying Preferential Payment to the Participants of Their Full Interests in the CCP.

The courts below recognized, as do the Trustees, that petitioners have legitimate executory contractual claims against Penn Central under the CCP.[5] These claims arise out of "services" rendered Penn Central *prior* to the institution of the reorganization proceedings. As a general rule, unsecured claims of this nature are not entitled to preferential payment during the reorganization proceedings, but are subject, as are other pre-reorganization claims, to determination as part of the proof of claim procedure and to disposition as part of the plan of reorganization.[6] As noted by the Court of Appeals, this is true whether or not petitioners' rights under the CCP became vested upon their respective retirements.[7]

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5. The Reorganization Court did not hold, as intimated by petitioner Bevan that this contractual claim was in any way affected by the establishment of the Reserve Fund. It merely determined that the CCP did not create any property rights in favor of Bevan in the Reserve Fund which would justify a preferential payment to him of his contractual claim. This misinterpretation of the Reorganization Court's decision, as well as many of the other statements and arguments made in the Petition at No. 73-584 are the result of Bevan's inability or refusal to accept the simple rule of bankruptcy law that unsecured contractual claims for services rendered prior to reorganization are not entitled to preferential payment during reorganization.

6. *Frasher v. Robinson*, 458 F.2d 492 (9th Cir. 1972); *Kooy v. Van Winkle*, 88 F.2d 481 (3d Cir. 1937).

7. The cases cited by petitioner Greenough at pages 9-11 of his petition merely hold that a pensioner has a vested contractual right to retirement benefits under a pension plan which cannot be terminated by the employer in the absence of a bankruptcy or reorganization proceeding. They do not purport to discuss the rights of a pensioneer as an unsecured creditor in a proceeding of this character and are not relevant to the issues before this Court.

The Reorganization Court, having concluded that the rights of Penn Central's retired employees under the CCP were merely contractual in nature, nevertheless authorized the preferential payment of limited benefits thereunder in accordance with the principles enunciated in *Bowen v. Hockley*, 71 F.2d 781 (4th Cir. 1934) and *Tate v. New York, N.H. & H.R.R.*, 332 F.2d 449 (2d Cir. 1964). These cases reflect a practice by railroad reorganization courts under Section 77 of the Bankruptcy Act, 11 U.S.C. §105, to authorize the continued payment of unfunded pensions falling due under a railroad's regular pension program.[8]

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8. In *Tate v. New York, N.H. & H.R.R.*, 332 F.2d 449 (2d Cir. 1964), the Court of Appeals reversed an order of the District Court in a railroad reorganization proceedings, which terminated payments to a retired executive of the railroad under a special contract providing reasonable retirement benefits ($13,000 a year) substantially similar to those payable under the railroad's formal pension plan, except that credit was given to him for service with a prior employer. The executive, in leaving his former employer, had forfeited all of his pension rights to date of termination, and it is a standard practice in the railroad industry to provide credit for prior service under such circumstances.

In *Bowen v. Hockley*, 71 F.2d 781 (4th Cir. 1934), the Court extended the rule to permit the continued payment during an equity receivership of a disability benefit awarded an injured employee prior to the institution of the proceedings under a state workmen's compensation statute. The debtor was self insured under the statute and the direct payments to the injured employee were considered to be in the same category of necessary operating expenses payable currently as would premium payments to an insurance company for coverage against future compensation awards during the receivership.

But, see *Alpert v. New York, N.H. & H.R.R.*, 348 F.2d 304 (2d Cir. 1965), where the Court of Appeals for the Second Circuit affirmed the denial of sums due a railroad's retired chief executive officer under his employment contract which provided for payment of $25,000 a year after retirement "by way of deferred compensation". The Court of Appeals drew a sharp distinction between contracts like Tate's, providing a pension similar to that payable under the railroad's regular pension plan, which should be paid for the purpose of maintaining and facilitating employee loyalty, incentive and recruitment, and contractual provisions for deferred compen-

The preferential payment of retirement benefits under *Tate* and *Bowen* is based upon the equitable factor of employee morale and not upon the contractual rights of the retired employees. Thus, the amount of pension authorized to be paid is not fixed by the terms of the contract or pension plan, but must be determined independently by the district court on the basis of equity and fairness under the circumstances. *Tate v. New York, N.H.&H.R.R.*, 332 F.2d at 452. Consistent with this teaching, the Reorganization Court, within its discretion, authorized the current payment of that portion of the participants' interests in the CCP attributable to the contingent compensation allotments (less prior payments under the CCP) and deferred consideration of the balance of their claims attributable to the increased value of the assets of the Reserve Fund until the adoption of a plan of reorganization.

In view of the extraordinary nature and limited coverage of the CCP and the fortuitous nature of the investment experience of the Reserve Fund, the Reorganization Court cannot be held to have abused its discretion in this regard. Petitioners have presented no sound reasons in any of their petitions for this Court to review the exercise of that discretion.

2. The Participants Have No Property Interests in the Assets of the Reserve Fund.

One of the arguments asserted in the Court of Appeals, and repeated by petitioners Bevan and Greenough

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Note 8—*Continued*

sation unrelated to the normal pension formula and serving none of these purposes. See also *Pyrites Co. v. Silica Gel Corp.*, 8 F.Supp. 423 (D.Md. 1934) (pre-receivership compensation denied to executives; granted to other employees); *In re Compania De Los Ferrocarriles De Puerto Rico*, 76 F.Supp. 521 (D.P.R. 1948) (pension discontinued as to executives; continued as to employees covered by labor contract); *In re Schenectady Ry.*, 93 F.Supp. 67 (N.D.N.Y. 1950) (pension suspended as to executives; continued as to employees covered by labor contract).

herein, is that they have more than mere unsecured contractual claims against Penn Central's estate. Rather, they assert a beneficial property interest by way of a trust—express, constructive or resulting—in the specific assets of the Reserve Fund and contend the courts below have improperly deprived them of their rights to those assets contrary to the decisions of this Court.[9]

The complete answer to petitioners' position in this respect is found in the CCP itself. Section 401 of the CCP provides:

> The Fund shall not be a trust fund and the assets therein shall be available at all times for any corporate purpose of the Company. A participant shall have no right in or to any funds or property which may be held in the Fund.

Section 1201 further provides:

> No participant nor any other person shall have any interest in any fund or in any specific asset or assets of the Company by reason of amounts contingently allotted to him. . . .

This language is as clear as can be and, as held by the courts below, sufficiently negates the existence of a trust relationship with respect to the Reserve Fund.[10] An ex-

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9. The petition in No. 73-584 relies upon the decision in *Pearlman v. Reliance Insurance Co.*, 371 U.S. 132 (1962). In *Pearlman*, this Court held that a Miller Act surety which had paid its principal's laborers and materialmen had an equitable claim for reimbursement out of the amounts retained by the United States to secure such payments, and that the principal's trustee in bankruptcy had acquired no property rights in the fund to the extent of the surety's equitable interest. The basis for the *Pearlman* decision, and all of the other decisions cited by petitioners Bevan and Greenough, is an identifiable fund or property in which the claimant can show a property interest, legal or equitable, superior to that of the bankrupt. As hereinafter discussed, petitioners did not have any property interest in the assets of the Reserve Fund entitling them to priority of payment of their entire interests in the CCP.

10. It is no answer to state, as Bevan has to this Court, that the clause making the assets available to Penn Central demon-

press trust cannot arise unless there has been an outward manifestation of intent on the part of the alleged settlor that the property should be held in trust (I Scott, Trusts §23, at pp. 190-91, §74.3, at p. 682 (3d ed. 1967)). *A fortiori*, there can be no trust relationship where the purported settlor has stated that no trust relationship is intended by his actions.

There was, moreover, no conduct on behalf of Penn Central contrary to the terms of the CCP. The Reserve Fund remained at all times in the custody of Penn Central's Treasurer available for corporate purposes, and was accounted for as an asset of the company. The mere fact that the officers of Penn Central, almost all of whom were participants, did not take advantage of the right to use the property in the Reserve Fund for general railroad purposes does not indicate that the intent of the Board of Directors was contrary to that expressly set forth in the CCP, nor does it indicate that the status of the property of the Reserve Fund was other than a corporate asset.

Petitioner Bevan's assertion that there is a resulting or constructive trust in the Reserve Fund, notwithstanding the terms of the CCP, because the contingent compensation allotments transferred thereto were the participants' property begs the question. The participants made no contributions of cash or property. Rather, in lieu of receiving their total compensation in the form of immediate cash salaries, they acquired contractual rights against Penn Central to receive deferred compensation after retirement to be measured by their interests in the Reserve Fund.

It is clear that the assets of the Reserve Fund remained at all times the sole property of Penn Central and were not

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Note 10—*Continued*

strates that the assets were not in fact the property of Penn Central, absent specific language to that effect. The respective rights of the participants and Penn Central to these assets can be based only upon the express provisions of the CCP, and petitioners can have no greater rights than are conferred under these provisions. *Boase v. Lee Rubber & Tire Corp.*, 437 F.2d 527 (3d Cir. 1970).

held in trust for the participants. As a consequence, the participants have no claim to these assets, but merely have a contractual right against Penn Central's estate. The decision of the Courts of Appeals denying participants' claim for priority is therefore not inconsistent with any decision of this Court and should not be reviewed by this Court.

3. The Reorganization Court Properly Exercised Its Discretion in Imposing the $50,000 Per Annum Limitation Upon the Payment of Unfunded Retirement Benefits.

The Reorganization Court in authorizing the preferential payment out of the Penn Central estate of unfunded pension benefits (including the partial payments under the CCP) limited the amount of benefits payable to any one former employee to $50,000 per annum. This limitation, affirmed by the Court of Appeals, is fair and equitable, and constitutes a proper exercise of the Reorganization Court's discretion which need not be reviewed by this Court.

The reasonableness of the $50,000 limitation is demonstrated by the analyses of the federal income tax returns filed for the years 1968 and 1969, published by the Internal Revenue Service,[11] which disclose that 99.6% of the wage earners filing returns reported adjusted gross incomes of less than $50,000 and an even greater proportion, 99.85%, in 1968, reported salaries or wages, as distinguished from total income, of less than $50,000.

An annual income of $50,000 should provide sufficient funds to maintain a comfortable standard of living, par-

11. Internal Revenue Service, Statistics of Income-1968, Individual Income Tax Returns, p. 27, Table 1.9 (1971); Internal Revenue Service, Statistics of Income-1969, Individual Income Tax Returns, p. 13, Table 1.4 (1971). The analysis of the federal income tax returns for the year 1970 discloses a similar percentage, 99.4% of total tax payers, as distinguished from wage earners, reporting adjusted gross income of less than $50,000. Internal Revenue Service, Statistics of Income-1970, Individual Income Tax Returns, Table 1 (1973). See also Fox, Top Executive Pensions-1969, The Conference Board Record, Vol VIII, No. 1, January 1971.

ticularly in retirement when a family's responsibilities are generally less. In view of the present financial condition of Penn Central, it would be highly inequitable to provide over-generous payments to retired employees out of Penn Central's estate while other claimants, many in hardship situations, are receiving nothing. As noted by the Reorganization Court, ". . . it would be unconscionable to permit the payment in full of all retirement and deferred compensation, no matter how generous the amount, while [Penn Central] is unable to pay current taxes. . . ."

The only specific challenge as to the fairness of the $50,000 limitation is petitioner Bevan's complaint that it discriminatorily limits payments out of Penn Central's estate to six executives while permitting full payment to all other retired employees of Penn Central under Penn Central's unfunded pension programs. As noted by the Reorganization Court, Bevan's suggestion that any limitation on payments should be on a pro-rata basis ". . . would . . . involve greater inequities than the flat limitation. . . ." and ". . . might make it difficult for retirees at the lower end of the scale to maintain themselves comfortably. . . ."

Petitioners have not stated any other ground for determining that the limitation is inequitable or that the Reorganization Court otherwise abused its discretion.[12] This Court, therefore, should not exercise its extraordinary jurisdiction to review that discretion.

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12. Petitioner Bevan, in arguing further that the $50,000 annual limitation constitutes an abuse of the Reorganization Court's discretion as applied to his interest in the CCP, merely reiterates the contentions made elsewhere in his petition that the assets of the Reserve Fund were the property of the participants, not Penn Central. As hereinbefore stated, the Courts below correctly decided that Bevan's rights under the CCP were solely contractual in nature and not entitled to any preferential treatment. This denial of preferential payment was without prejudice, however, to Bevan's right to assert his claim thereunder as part of the proof of claim procedure instituted in the reorganization proceedings.

CONCLUSION

For the above reasons, it is submitted that the refusal by the Reorganization Court to grant petitioners preferential payment of their entire interests in the CCP is not inconsistent with any decision of this Court, and that the limitation imposed upon the payment of unfunded retirement benefits payable to petitioners did not constitute an abuse of the Reorganization Court's discretion. The affirmance of Order No. 1087 by the Court of Appeals was therefore correct and need not be reviewed by this Court. The Petitions for Writs of Certiorari filed by petitioners should be denied.

Respectfully submitted,

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